Hearing before the
United States House of Representatives,
Committee on Financial Services

The Dodd-Frank Act at Five Years:
Are We More Free?

September 17, 2015

Statement of Amb. C. Boyden Gray

I am grateful for the opportunity to testify before this Committee, on the fundamental constitutional problems inherent in the Dodd-Frank Act[1]—both in the Act's structure and in the manner in which federal agencies are administering it.

I have had the honor of testifying previously on these issues several times since Dodd-Frank was enacted five years ago. Just two months ago, for example, I testified before a subcommittee of the Senate Judiciary Committee on the constitutional flaws inherent in Title X of the Act, which created the Consumer Financial Protection Bureau (CFPB).[2]

And in 2013, for example, I addressed the similar structural constitutional flaws of Dodd-Frank's Title I (creating the Financial Stability Oversight Council, or "FSOC") and Title II (creating the Orderly Liquidation Authority, or "OLA"), before

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1 Pub. L. No. 111-203, 124 Stat. 1376 (2010).

2 *The Administrative State v. The Constitution: Dodd-Frank at Five Years*, 114th Cong. (July 23, 2015), *available at* http://boydengrayassociates.com/ambassador-gray-testifies-on-the-constitutionality-of-dodd-frank-and-the-consumer-financial-protection-bureau/.

the House Financial Services Committee's Oversight and Investigations Subcommittee.[3]

But most importantly, I am co-counsel to several parties litigating a constitutional challenge to the CFPB, to Director Cordray's recess appointment, and to FSOC in federal court; alongside us in that case are States challenging the Orderly Liquidation Authority. The day after I testified in July as to the CFPB's unconstitutionality, the U.S. Court of Appeals for the D.C. Circuit issued a decision recognizing our legal standing to litigate the merits of our constitutional claims against the CFPB.[4] We look forward to finally reaching the substance of these crucial constitutional issues in court. But I also appreciate the opportunity to discuss them here today, in the hopes that Congress itself will remedy Dodd-Frank's constitutional violations.

It is no accident that a community bank is the lead plaintiff in our case: community banks have been hit very hard by the CFPB's unchecked powers, and unlike Wall Street banks they cannot simply hire an army of lawyers and lobbyists in perpetuity. Just as big government and bureaucratic discretion inherently favor the biggest businesses over small upstarts, so community banks—and the communities and Main Streets they serve—bear the brunt of the CFPB's regulatory onslaught.

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[3] *Examining Constitutional Deficiencies and Legal Uncertainties in the Dodd-Frank Act*, 113th Cong. (July 9, 2013), *available at* http://www.boydengrayassociates.com/examining-constitutional-deficiencies-and-legal-uncertainties-in-the-dodd-frank-act/.

[4] *State Nat'l Bank of Big Spring v. Lew*, 795 F.3d 48 (July 24, 2015).

Because I have already testified in detail as to Dodd-Frank's constitutional problems, I incorporate those testimonies by reference. (Their full text is available online, as noted above in footnotes 2 and 3.) As I explain there, each of those statutes violates the Constitution's separation of powers, its checks and balances, and each raises a host of other constitutional or practical problems. Let me briefly summarize the general constitutional issues here:

In Title X, Dodd-Frank creates the CFPB with an unprecedented combination of independence from both the Executive Branch and the Legislative Branch; it adds to that combination an open-ended delegation of regulatory power, and it orders the federal courts to give extra deference to the CFPB's interpretation of its statutory powers.

In Title I, Dodd-Frank creates the FSOC and vests it with open-ended powers with respect to "systemically important financial institutions" (SIFIs), while also severely limiting the courts' jurisdiction to review the FSOC's SIFI determinations. Indeed, Dodd-Frank expressly limits the courts to reviewing only whether FSOC's findings are "arbitrary and capricious,"[5] and thus seems to restrain courts from their normal, fundamental duty to review not merely whether an agency's work is "arbitrary and capricious" but also whether it is "in accordance with law."[6]

And in Title II, Dodd-Frank creates the OLA and vests the agencies administering it with unprecedented powers and discretion over the financial system. OLA replaces traditional court-managed bankruptcy with a process

[5] 12 U.S.C. § 5323(h).

[6] 5 U.S.C. § 706(2)(A).

controlled by executive branch officials and other unaccountable regulators. It subjects the process to aggressive gag rules preventing even investors from knowing what is happening to companies before it is too late. And it imposes draconian restrictions on judicial review: the courts may review only whether the company is a "financial company" and whether it is "in default or in danger of default"; the courts are *not* allowed to review the government's finding that the company's possible default would "have serious adverse effects on financial stability in the United States."[7] Furthermore, Dodd-Frank sets an infeasible 24-hour deadline for the district court to hear the case and decide whether to stop the government from liquidating the company; once that strict 24-hour clock expires without a district court decision (as it certainly will), the government automatically wins and may begin liquidation.[8] And in liquidation, the government does not need to honor the century-old laws guaranteeing the equal treatment of similarly situated creditors; the government instead can pick and choose winners and losers[9]—as it did in the Chrysler and GM crises, ultimately forcing the State of Indiana's pensions to swallow immense losses. This regulatory framework raises myriad constitutional problems: its combination of independence from Congress (which has no "power of the purse" over the OLA) and from the courts (which exercise no meaningful judicial review of the OLA), combined with the statute's grant of open-ended powers, raises significant separation-of-powers questions. It also raises serious questions under

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[7] 12 U.S.C. § 5382(a)(1)(A)(iii).

[8] 12 U.S.C. § 5382(a)(1)(A)(v).

[9] 12 U.S.C. § 5390(b)(4).

the Fifth Amendment (which guarantees due process) and Bankruptcy Clause found in Article I, Section 8 of the Constitution (which requires that bankruptcy laws be "uniform").

In addition to these points about Dodd-Frank's structural unconstitutionality, I would like to add one more point regarding the nature of the agencies' regulatory approaches. As I discussed recently in the *George Mason Law Review*,[10] Dodd-Frank does not require the FSOC to justify its SIFI designations by demonstrating that the designated financial company poses a substantial *likelihood* of causing systemic financial harm; rather, it allows the FSOC to designate a financial company as a SIFI if it merely "*could* pose a threat to the financial stability of the United States."[11]

That open-ended grant of power, which fails to require the FSOC to show that its SIFI designations are actually necessary to avoid a significant risk of harm to the public, ignores the Supreme Court's emphatic admonition that statutes must not be construed to allow an agency to impose substantial regulations without evidence that such regulation is actually necessary to prevent significant risk of harm. To allow otherwise would be to "make such a 'sweeping declaration of legislative power' that it might be unconstitutional under" the Court's nondelegation precedents, as Justice Stevens' plurality opinion in the *Benzene*

[10] *The Nondelegation Canon's Neglected History and Underestimated Legacy*, 22 Geo. Mason L. Rev. 619 (2015).

[11] 12 U.S.C. § 5323(a)().

Case explained. "A construction of the statute that avoids this kind of open-ended grant should certainly be favored," he and his colleagues stressed.[12]

The Court reiterated this approach in *Whitman v. American Trucking Associations,* where it narrowly construed the Clean Air Act's Section 109(b)(1). That statute provides for the establishment of air quality standards that are "requisite" to protect public health. The Court, at Solicitor General Waxman's own urging, construed this as authorizing the EPA only to set standards that are "sufficient, *but not more than necessary*," to protect public health.[13]

The FSOC's regulatory approach, pursuant to Dodd-Frank's Title I, heeds none of these warnings. It recognizes no need to show actual, *significant* risk of systemic financial harm before designating new SIFIs—and its SIFI designations to date show no such significant risks of public harm actually being prevented. The FSOC claims power to make SIFI designations, with immense ramifications on our economy, based on *sheer speculation*—precisely the nondelegation violations that the Supreme Court warns emphatically against.

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Thank you, again, for the opportunity to testify on these crucially important issues. I welcome your questions.

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[12] *Industrial Union Department, AFL-CIO v. American Petroleum Institute (“Benzene Case”)*, 448 U.S. 607, 646 (1980) (plurality op.). Justice Rehnquist did not join the plurality opinion, but he echoed the plurality’s point regarding the prohibition against agencies claiming power to regulate insignificant risks, when he expressly agreed that the agency cannot claim power to “eliminate marginal or insignificant risks of material harm right down to an industry’s breaking point.” *Id.* at 683 (Rehnquist, J., concurring).

[13] *Whitman v. Am. Trucking Ass’ns*, 581 U.S. 457, 473-74 (2001) (emphasis added).